RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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August 13, 1986 **LETTER 945**

August 1 DJIA 1763.64; PTI 2314; A-D Ratio -7.54
August 8 DJIA 1782.62; PTI 2314; A-D Ratio -7.76

THE PICTURE: I'll probably never write another Letter like this one, but please, just this once let me have my way. A fair-sized chunk of this Letter (see inside) is in response to my friend Harry Schultz's latest report. I thought subscribers might be interested in both Harry's ominous view of the future and my answer.

I guess another reason I wrote such a long section is because I read a lot of newspapers (about eight a day), and a lot of the things I read today bother me. And I sit here, and I think, "Is America going nuts? Have we lost our collective mind? Why are our leaders spending all their time fussing and arguing about a new tax bill (which looks to me to be as messy as the old one) while the nation's deficits keep climbing and our balance-of-payments become a total disaster? And why are we all fired up about South Africa (remember when it was Iran and then Nicaragua) even though we don't really have any answer for Africa?" (I've been studying S. Africa for 25 years, and I swear I still don't know what the solution is. But I know one thing -- dumping shares in S. African industry (divestment) isn't going to do a damn thing. I sell my S. African shares to somebody else who buys them cheaper, and what have I done for S. Africa's blacks or anyone else on the African continent? Answer: nothing.)

I look through the papers and I see that LTV has filed for chapter 11, Bethlehem Steel (which used to be AAA-rated) has passed the dividend on both its common and its preferred (and on top of that the USX steelworkers are going to go out on strike, do you believe it?), the US trade deficit is predicted to be a negative $170 billion for the full year (is that grotesque?!), CBS sees a "substantial reduction" in network profits, Volcker tells Congress (for the umpteenth time) that "the Fed can't do it all," and the dollar breaks to new lows (but what's so ominous is that even with the new lows in the dollar, it seems as if Americans still want to buy only foreign goods).

Anyway, if you want discouraging news, today's newspapers can give it to you. And as I said, I read eight papers a day, and I have a good memory, so I can cite chapter and verse on today's bad news. I can scare you to death with how this country is fouling up — both in its domestic and in its foreign policies.

But however much I know about the US's troubles, the market knows more -- much more. The stock market is aware of more horror stories, more tales of fiscal and monetary woes, than you or I could read about in ten lifetimes. So why don't we turn to the market and see what it's doing and saying?

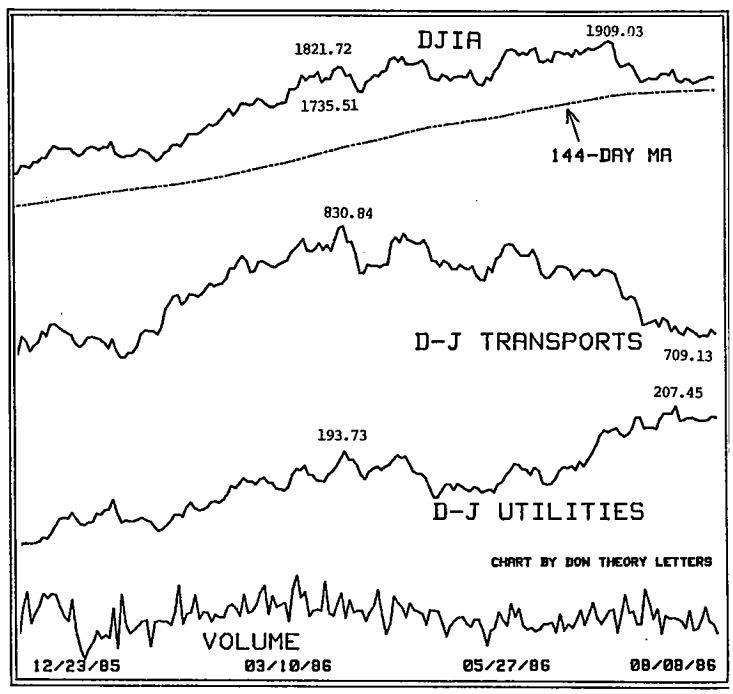
I've said it in previous Letters, and I'll say it again -- I think the stock market is fated to be stuck within A BROAD TRADING RANGE, a range probably bordered by the recent (July 2) Dow high of 1909.03 and roughly 1600 (that's my educated guess) on the downside. I have felt this way (about the trading range) for a number of reasons. First, we had the three big "buying stampedes" starting in December 1984 and lasting through to late-March 1986. Now three major buying stampedes can chew up an awful lot of buying power, and I feel that's exactly what happened during the 1984-86 breadth explosion (these buying stampedes were discussed in detail in the Letters of 1985 until early-1986).

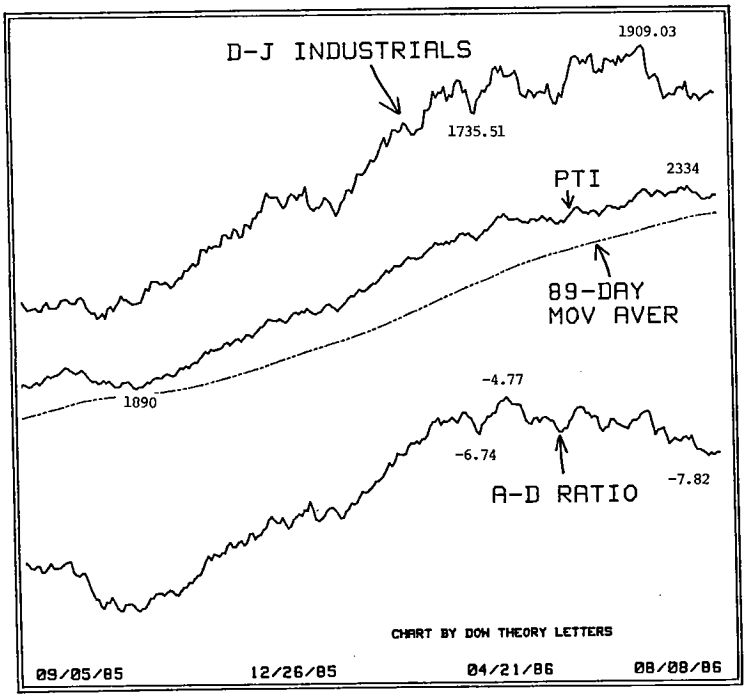
Next, we began to see some topping-out action in the various averages and indices. First we saw the D-J Transportation Average peak out at 830.84 on March 31. This was followed by an April 21 peak on the advance-decline ratio (and you can see this clearly on the page 2 chart). Following that action, the D-J Industrial and Transportation Averages began diverging -- with Industrials recording a series of new all-time highs even while the Transports were sliding to new lows. On July 2 the D-J Industrial Average recorded an all-time (unconfirmed) high of 1909.03. My guess is that this high will stand for quite some time. Or if it is bettered, it will be bettered only slightly.

Incredibly, during most of this topping out process my PTI continued to rally. In fact, from April 21 to July 25 the A-D ratio and the PTI diverged steadily, a performance that is as rare as it is unusual (see page 2 chart). Finally, on July 25 the PTI recorded its all-time high of 2334. I now consider it crucial to see whether the PTI forms a definite downtrend -- or whether it continues to resist on the downside. If the PTI traces out a definitive downtrend (i.e., holds below a declining trendline), this correction will undoubtedly become more severe.

So far, the broad market (as measured by the A-D ratio) has been in what must be considered a mild slide. As of last week the A-D had given up just a little over 3 points. Considering the dismal economic news, this doesn't represent too much in the way of a loss, particularly when you consider that the A-D advanced 11.46 points from its October 1985 low to its April 1986 high. In other words, the A-D (which is a proxy for ALL the stocks on the NYSE) has given up roughly 25% of its most recent gains.

I continue to feel that the key to the downside for this market resides in the ACTION OF THE DOW itself. The Dow (along with the PTI) led the market on the advance, and the Dow has been the main "resisting force" during the decline. A key downside level for the Dow is the 1735.51 low of April 7. So far, the Dow has not CLOSED below that level, even though it did drop below 1735.51





on August 4 on an intra-day basis (the Dow was down 26 points during that day, but it closed up 6 points in a dramatic one-day reversal rally).

Should 1735.51 be penetrated on a closing basis, I would look for the Dow to possibly test the area of its 200-day moving average. The 200-day MA now stands at 1670.

So that's the market picture as of this writing. Actually, a mild correction so far, but a lot of accompanying emotion (much of the emotion being caused by the violent and dramatic fluctuations in the Dow). On the face of it, I would expect the market to correct further on the downside, but I'm not going to attempt to outguess Wall Street. I continue to feel that the most logical thing to expect from here is a broad (frustrating for traders) TRADING RANGE.

Question: How could the market issue a Dow Theory bear market signal, given the current structure?

Answer: At this point, I feel that both Averages, the D-J Industrials and Transports, have gone far enough in both DURATION and EXTENT on the downside, so that we can say that they have traced out full secondary corrections. From the 1909.03 peak of July 2 the Industrial Average has now declined 146 points in a period of just over one month. From its March 31 peak of 830.84, the Transports have now given up 121 points in a period of five months. As I said, in both duration and extent I now feel that both Averages have now completed part or all of a secondary correction.

What the Averages do from here is of crucial importance. Somewhere ahead we are going to witness a rally -- or if you will -- a full (upward) correction of the decline so far. If, on that rally, one or both Averages fail to go to new highs, that will be a danger signal. If, on the ensuing decline BOTH Averages break whatever lows are now being established, then a primary bear market will be signaled.

Question: If such a bear signal materializes, will you pull the bull out of the box and issue an all-out sell signal?

ANSWER: If this market starts rallying in earnest (and I think it will somewhere between now and the end of the year) and if I do not like the upside action I am going to suggest utmost caution and probably some selling (this would be my first real sell recommendation in a long time). The fact is that, technically, a lot of things in this market are now "out of whack," and that is really the reason I have been talking about a wide and extended trading range.

If a primary bear market is signaled somewhere ahead, it is my guess (and this is only a guess) that the bear market would probably take the Dow down to the lower area of my predicted trading range. Thus, for the sake of argument, if the Dow rises to 1900 or above and the general market action remains weak (many non-confirmations), I would expect a bear signal and probably (again my guess) a limited bear market. My expectation would be that such a bear market would probably carry the Dow down to the 1600 area or thereabouts.

Question: Russell, isn't it dangerous to attempt to predict how far a bear market will carry on the downside?

Answer: You bet it is, and that's why I would probably recommend extensive selling in the event of a true bear signal. However, because the background economic news has been so poor, and because there is already so much caution built into the current situation, I am guessing that the stock market has already absorbed a good deal of pessimism and selling. That is another reason why I feel that the 1900 to 1600 range is going to contain the Dow for many, many months to come. In my opinion, we have entered a period of confusion and frustration -- a period that will prove to be particularly difficult for traders. I expressed those same sentiments a few months ago, and I am repeating them now. The easy part of this bull market has PASSED.

INVESTMENT POSITION: The bull stays in the box, but he's obviously a bit battered. There's been a ton of bad news over the last few months, and in the face of it this market has not been acting too badly. Bull markets don't tend to collapse amid bad news, but what with deflation, a swooning dollar, 31 states in recession, outrageous federal deficits and pathetic balance-of-payments statistics, we've already had enough bad news to send this market careening to lower levels. But as I said, the market has not been acting too badly, suggesting that a lot of rotten news has already been absorbed.

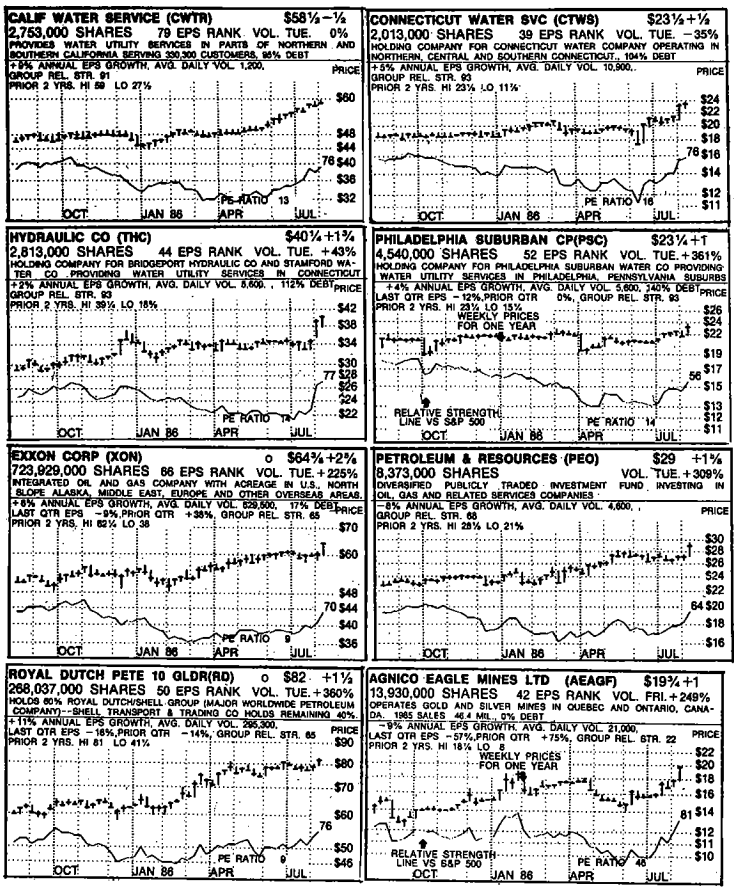
The best and most profitable policy all along has been to sit tight with HIGH-GRADE stocks and bonds. I want to stress again (as I have all along) that the operative words are (1) high-grade and (2) income. Why do I say that? Because high-grade (or safe) income is what you want when the market becomes shaky, and high-grade income is what is going to pull us through when the going gets rough.

When everyone is loaded with junk bonds and OTC cheapie stocks, I want to be on the other side of the fence. In other words, I want to own top-rated bonds and high-grade (quality) stocks. And that's exactly what I've been recommending, and nothing else

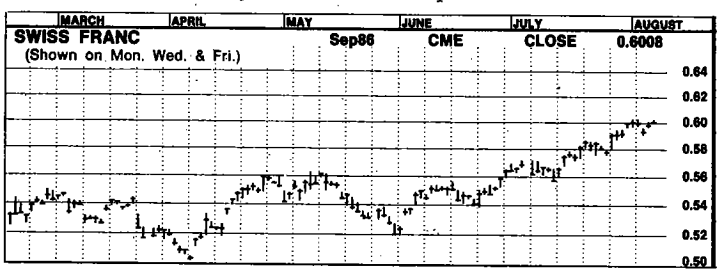
Throughout the market decline, the utility shares have been stars. And this is particularly true of the oft-recommended water utilities. Last week four of the water stocks hit new highs, and they are shown on the charts below. Crude oil jumped 50% in price in two days (Aug. 4 and 5) and the three oil stocks that I have recommended (Exxon, Royal Dutch, Petroleum Resources Pfd.) all went to new highs. I show the charts below, but remember on Petroleum Resources I recommended only the convertible preferred -- which is a relatively safe investment with a good yield plus a play on an oil recovery (the preferred is traded on the NYSE). All charts are from Investor's Daily.

Do no more buying, however. Let's sit tight and see how this market acts over the next few months.

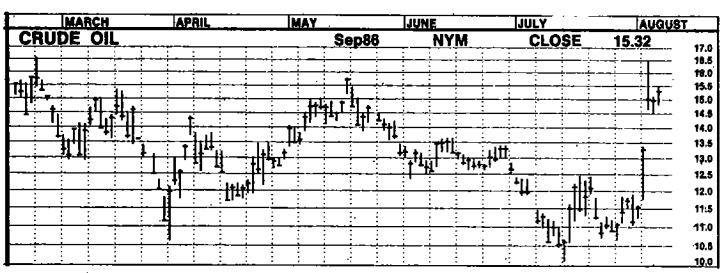
Charts -- see page 3.


CALIF WATER SERVICE (CWTR) $58⅛−½
2,753,000 SHARES 79 EPS RANK VOL. TUE. 0%
PROVIDES WATER UTILITY SERVICES IN PARTS OF NORTHERN AND SOUTHERN CALIFORNIA SERVING 330,300 CUSTOMERS, 95% DEBT
CONNECTICUT WATER SVC (CTWS) $23¼+½
2,013,000 SHARES 39 EPS RANK VOL. TUE. −35%
HOLDING COMPANY FOR CONNECTICUT WATER COMPANY OPERATING IN NORTHERN, CENTRAL AND SOUTHERN CONNECTICUT. 104% DEBT
HYDRAULIC CO (THC) $40¼+1¾
2,813,000 SHARES 44 EPS RANK VOL. TUE. +43%
HOLDING COMPANY FOR BRIDGEPORT HYDRAULIC CO AND STAMFORD WATER CO PROVIDING WATER UTILITY SERVICES IN CONNECTICUT
PHILADELPHIA SUBURBAN CP(PSC) $23¼+1
4,540,000 SHARES 52 EPS RANK VOL. TUE.+361%
HOLDING COMPANY FOR PHILADELPHIA SUBURBAN WATER CO PROVIDING WATER UTILITY SERVICES IN PHILADELPHIA, PENNSYLVANIA SUBURBS
EXXON CORP (XON) o $64¾+2⅛
723,929,000 SHARES 86 EPS RANK VOL. TUE.+225%
INTEGRATED OIL AND GAS COMPANY WITH ACREAGE IN U.S., NORTH SLOPE ALASKA, MIDDLE EAST, EUROPE AND OTHER OVERSEAS AREAS.
PETROLEUM & RESOURCES (PEO) $29 +1⅛
8,373,000 SHARES VOL. TUE.+309%
DIVERSIFIED PUBLICLY TRADED INVESTMENT FUND INVESTING IN OIL, GAS AND RELATED SERVICES COMPANIES
ROYAL DUTCH PETE 10 GLDR(RD) o $82 +1½
268,037,000 SHARES 50 EPS RANK VOL. TUE.+360%
HOLDS 60% ROYAL DUTCH/SHELL GROUP (MAJOR WORLDWIDE PETROLEUM COMPANY)--SHELL TRANSPORT & TRADING CO HOLDS REMAINING 40%.
AGNICO EAGLE MINES LTD (AEAGF) $19¾+1
13,930,000 SHARES 42 EPS RANK VOL. FRI.+249%
OPERATES GOLD AND SILVER MINES IN QUEBEC AND ONTARIO, CANADA. 1985 SALES 46.4 Mil., 0% DEBT
OCT JAN 86 APR JUL

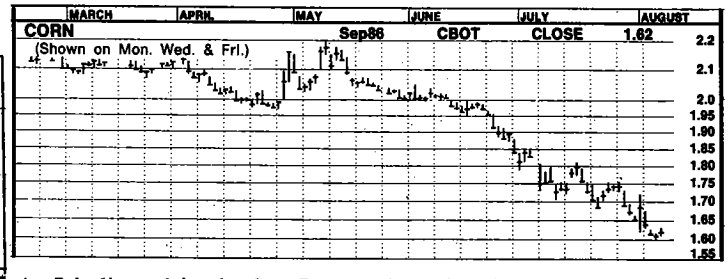
CRUCIAL CHARTS: Since April the foreign currencies have risen "big" against the dollar. Here we see the Swiss franc on its great June-August rally. If Swissie breaks .58 on the Sept. contract, then the dollar is in for a major reversal to the upside. Let's watch it.



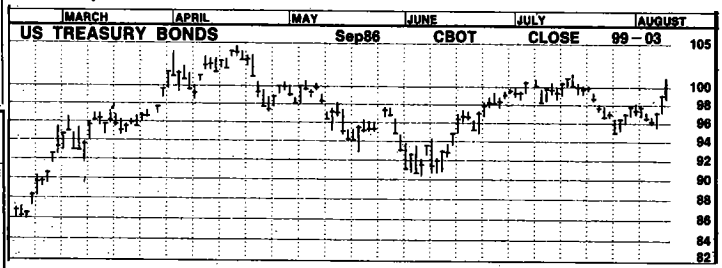
The Sept. crude oil contract shows the kind of explosion one sees in a commodity maybe once in a decade. There should be a lot of backing and filling and vibrating following the August oil explosion. Of course, whether the oil rise sticks depends on whether OPEC can get its act together (most of the skeptics think they can't, but I think they can). At any rate, the market (so far) thinks the OPEC oil cutbacks are for real.



Life on the farm is rough these days. And if you farm corn or soybeans it's been more than rough -- it's been a disaster. This daily chart shows the unbelievable smash in corn, the nation's biggest cash crop.



As I indicated in the last Letter, the T-bonds appear locked in a high-altitude trading range. My guess is that they'll stay there for quite a while -- or as long as the Japanese continue to take in US Treasury debt.



THINKING IT OVER: I've known Harry Schultz a long time. I knew him before he had an advisory service (at the time he owned I think it was 13 newspapers here in Calilfornia). At any rate, for reasons of his own Harry sold his newspapers and went into the advisory business -- that was around 1961. And Harry Schultz has been a big name in the advisory business ever since (the Wall Street Journal once did a full front-page story on Harry, and I don't think they ever did that for any other advisor).

In his latest report, Harry published a page 1 article that included a letter to me. I felt like answering that letter, and I felt that my own readers might be interested in the answer. My answer is a long one, and I guess getting out of the hospital and escaping the black angel might have had something to do with my writing this thing. But anyway, I'm reproducing the piece from Harry's report exactly as it appeared, and then comes my answer. I hope you find something in it that means something to you. Thanks for indulging me.

(The next is from the International Harry Schultz Letter, late-July 1986.)

Big picture I have a feeling of *foreboding*. That things R going to get *VERY bad VERY soon*. And with bitter irony, I note that after having predicted all the problems we now have, & those which R unfolding daily, I've not taken enuf precautions & will be caught in the maelstrom. Shoemakers' children go w/out shoes. I feel this so strongly I cant even write a friendly birthday note to an old friend w/out voicing my concern. Richard Russell & I have been writing to ea other (& occasionally meeting in restaurants) for 22yrs. I've known 3 of his wives & he has known 2 of mine. I'm Godfather to 1 of his kids. Here is a letter I enclosed w/a birthday card I sent him 10days ago:

"To: Richard the Russell. July 11th. ..Dear pal Dick, I must warn U that yor birthday is coming up. Be prepared for another burst of wisdom. ....R U the fellow that's married to the famous Faye I read about in *Dow Theory Letters*? Your Letter gets better, mellower, like a fine wine, improving with age. I really enjoy it.

World wise: I'm coming to the opinion the whole scene will *disintegrate* before too long. Deflation, depression, credit crash, banks closure, runaway Aids plague, US exchange controls, Orwellian new $-bills, earthquakes (Calif flattened? RR moves to Monte Carlo?), SoAfr cut off by USSR so West is at mercy of USSR, BigBrother supremacy over the individual. I fear a gooey mess soon, *where we all lose*. Society decimated. All resulting from immorality: first of currency,

then of people (cause&effect). The good days of freedom to travel, seminars, prosperity, nice restaurants & laughs may soon be a memory. A *new Dark Age* looms. .Any other view is Pollyanna, IMO.

I wish U wud get more involved in freedom fighting. Not just observe, but take part, before U R not *ALLOWED* to comment anymore. ...I bet U have no fall-back plan to exit San Diego, the USA, banks, etc..... But for this year at least, *or JULY anyway*, it's safe to wish U a happy birthday... your old pal, Harry. ..PS: (censored) is in process of moving out of the US (not yet for publication), is in fact moving to Monte Carlo! Sez he is getting out ***before the gates close***! That will make 4 newsltr writers living here. Another in UK is considering it. Want to join us?" (Atlas Shrugged)

Here's my answer, Harry. Sure I'd like to join you, but it could only be for a few weeks. Then it would be back to the USA for me. Harry, I know you've been saying for years that the US is heading for major trouble. And I'm not going to argue with you, because I'm afraid you could be very right. And Monte Carlo sounds fabulous, and what's more I've got the wherewithal now to pack up and move to Monte Carlo and well -- to retire there. We'd probably have the time of our lives, but I can't do it. And I'll tell you why in a single sentence: My heart (I've been talking a lot about hearts lately) is rooted here in the US, Harry. If Monte Carlo was paradise itself (and it may well be) I still couldn't leave. My roots are too deep, Harry, they go down into half the states of the union.

Let me tell you something about my family history. My ancestors came over from England back in the 1700s. One of my way-back, great-great-great grandfathers was named Abraham Alexander, and he was an officer in General Washington's army. He was a Jew, which makes me a kind of a rare bird, a Jewish Son of the American Revolution (yeah, I have the papers to prove it). My great-great grandfather was killed in the battle of Manassas during the Civil War. (He fought on the losing side, but it was his side of America, and he died for it.) My grandfather owned the biggest jewelry store in Charleston, SC, and when the stock market collapsed back in 1902 during the Northern Pacific Panic, that proved too much for grandpa. He had lost most of his money. And I guess he couldn't face what he thought was a disgrace. So grandpa took out his Colt (he used to sleep with it under his pillow) and blew his brains out. That happened around 5am of a quiet Charleston morning. I know because my dad told me about it. He was only 8 when it happened. He heard the gun shot at 5am. Then he tip-toed into the living room, and there was his daddy lying in a pool of blood, slumped over his mahogany desk. After that my dad woke up every morning at 5am for the rest of his life. It was like -- here's 5am and pow, Dad sat up, fully awake! I loved my dad, and I always saw as much of him as possible. And that's how I got into my own lifelong habit of waking up early. I still get up around 4 to 5am every morning (as if my early-rising dad was still here). Strange story, isn't it, Harry? I guess that gunshot is still echoing. Hey, you want to know something funny? I just realized that your name is Harry and so was my dad's, although everyone called him Harold.

My dad was in the Naval Air Force during WW I. He flew anti-submarine duty in those big WW I seaplanes. My dad was a civil engineer, and just about the time he graduated from Columbia University the Great Depression hit. So Dad couldn't do what he loved best -- construction (because there was no building during the Depression). So he managed NYC real estate instead. My father taught me one thing well, and he believed it deeply: he used to say, "Dick, every problem has an answer. You just have to get out there and keep after it until you find it." That was some of the best advice I ever received.

The stock market part of the story goes further. My father's half-brother, Irving, had a lot of family money. He was sort of a playboy, and he used to date pretty NY chorus girls (it was a sort of family scandal). When the crash of 1929 struck Irv's income dropped in half, and that shock was too much for him. One day in 1929 he jumped to his death out of a hotel window. But he left me a good sum of money in his will. I got that money when I turned 21, and it was learning what to do with that money that originally got me interested in the stock market. My uncle Irving's pathetic death had a major effect on my life. God has his ways.

Then I guess you know, Harry, that I was a flyer for the Army Air Force during WW II. I was a bombardier with the 12th Air Force in Italy, and I was having the time of my young life until the flak started coming at me. Around 1944 the rumor went among the crews that the Germans would kill all Jewish bombardiers on sight. That's when I started packing two pistols instead of one. I could tell you a real carload of war stories, Harry, but let's drop it at that. Let's just say that once I got into the shooting part of the war, the fun was over, and I mean o-v-e-r.

What about my mom? She lives here in La Jolla, about 10 blocks away. She's been around for a long time (she won't let me say 88 years), but she makes great chicken soup and even better bread pudding -- loaded with fruit. Mom can tell you what NYC looked like before there were cars and what life was like before the radio. Mom graduated from Hunter College when it wasn't fashionable for girls to graduate from anywhere. Mom is also a writer. She's had four novels published (one on the NY Times' best seller list), but she's taking it easy now -- except for worrying about me. And boy, can she worry!

Harry, believe me, all this is just a very abbreviated story of my family. But what I'm trying to tell you is that I'm so rooted here in history, family, and emotion that it would take earthquakes, fires, starvation, and an American Hitler (and I don't think that's going to happen) to get me to leave this country.

On top of all the foregoing, I've got five kids that I see whenever I can. I've got three grown girls with my first wife. One's Daria, who's 31, works at KPBS-TV here in San Diego. She's a free soul and a hard worker, and she just got married (a few weeks ago) to a very nice guy. He's a safety officer for PSA. He comes from a little town in S. Dakota and his background and my daughter's couldn't be more different. But as they say, "That's what makes America." My first wife, whom you knew, was the daughter of Max Lerner, the well-known liberal writer and philosopher. Anyone who lived in the East during the 1940s to '60s knows Max well. Max is in his 80s now, and I love him. Max and I still correspond, and we see each other when we can. My second daughter, Nicole, is autistic (schizophrenic). Nicole lives in a strange dark world, and she won't let me or anyone else into that world. Nicole is well over 20, Harry, and she's never talked. But she's very sensitive, and we're sure she knows things other people don't know. She resides with her mom in Pacific Beach, a few miles south of here. Her mom runs a sort of religious-psychological commune. People work there, and share their lives with each other. I tried it for a while, and it was interesting, but I like my privacy, so I left. But it was quite an experience. I guess I was a sort of '60s hippie, at least for a while.

My third daughter is a 22-year-old actress named Betsy Russell. Betsy lives in Hollywood, and she's the glamor girl of the family. I wouldn't let her near you Harry, because you'd probably try to run off with her (she's that good looking). Betsy lives with a handsome guy named Jeff. He's in real estate, not acting -- for which I'm thankful.

My second wife is named Paula, and you know her too, Harry. She's a real Western American type. Her grandpa was sheriff of Joplin, Missouri (a very tough town in its day), and her mom is a musician. Mom helped organize Fred Waring's musical group, but now, at 70, she plays in night clubs in San Bernardino. Mom can play and sing any song you've ever heard of. We used to play a game of, "Can you remember this one?" Mom always remembered, and always beat me. Paula grew up in Palm Springs and she was a runner-up to Miss Palm Springs back in the '60s. She was also a stewardess for American Airlines in the days when the stews were all gorgeous -- remember? Paula was a beauty then, and she's one now. She was also a heck of a businesswoman and was vice president of a conglomerate when I met her. We have two kids, Ryan, age 8, and Lauren. Harry, you know Ryan because you're

his godfather. Ryan has spanking blue eyes, he's my only boy, and he loves baseball, soccer and fishing. Then I have a little girl, aged 5, named Lauren. She's a blond beauty, and if her brains ever match her looks she'll be running GM some day. Right now Lauren's busy falling off things. Last week Lauren broke her wrist falling off a slide. Last year Lauren broke her elbow falling off a bannister. She keeps the hospitals here plenty busy.

Paula and I are still pals, but we're just in different worlds. Paula likes to travel, to sparkle, to dress up, to rush and run. I like to think, to stay in one spot, and to talk to people on a deep level. Paula always felt I was "too heavy." She was probably right. But she taught me how to have fun (believe it or not, I grew up not knowing how to have fun!). In turn, I taught Paula how to face things that are hard to face. We're buddies now, and I don't think either of us have any regrets about anything.

Harry, I think God finally began to feel a little sorry for me. He said, "Russell, you've been in one form or another of psychotherapy for 30 years. You started out unhappy and kind of crazy, and now I'll have to admit that you're doing a heck of a lot better. I'll tell you what I'm going to do, Russell. I'm going to give you a final chance to get it right. When you go down to the La Jolla beach tomorrow you're going to meet a girl. Her name is Faye Hunter. She's real pretty, she's got reddish-blonde hair -- you can't miss her. She went to La Jolla High and she graduated from Stanford. She's got twice your brains, and she'll talk to you about anything from anthropology to the latest fall fashions to the war in Afghanistan. And she's very calm and collected -- which should be just the ticket for a nut like you. There's only one problem. She's 30 and you're 62. But listen, I never said I was going to give you a rose garden. I said I was going to give you a chance to get it right -- and this is it, jerk. So you better grab it."

So, Harry, I went to the beach the next day, and I met Faye. But I was a bit slow. I didn't call her for two months because I thought maybe she was too young for me. But two months later, a girl who knew Faye well said to me, "Hey Richard, remember Faye Hunter, the girl on the beach? She liked you. Why don't you call her?" I called her an hour later, and we had our first date that night at a local Chinese restaurant. We haven't been apart since.

Harry, I can't pack up and leave the US. I don't know if all the foregoing tells you anything specific, but it probably gives you some hints. I know things are kind of insane here in the US. We've spent ourselves into debt for the next hundred years, we've mortgaged ourselves to the hilt. We can't protect our borders, and it seems like the whole country is on coke or crack or pot or you name it. Now the AIDS plague has hit, and our farms are going under, and the Japanese and Germans are beating the hell out of our manufacturers. But with it all, this is where my heart is Harry, and if the ship is going down I guess I'm going to go with it. In the meantime, I'm writing my head off as usual, trying to do some good, and trying to get a few ideas across.

Harry, I know you probably disagree with me, but the US is where the "Freedom Buck" stops. If this country can't survive one way or another, then I don't know how I'm going to survive or my family is going to survive either. The US has one interesting habit — we shoot dictators here, and we overthrow the would-be monsters. Huey Long was shot dead, and McCarthy was beaten to a pulp in court. People here are slow to move and slow to make changes. But ultimately, at least up to now, they somehow always get around to doing the right thing. Harry, don't ask me how it's all going to work out. Because I don't know, and I'm not even sure it can work out.

I'm a football fan, and they don't play football in Monte Carlo. That's one thing that worries me about moving. The other is that my family has had too much blood spilled on American soil. My daddy is buried in a Queens graveyard just outside NYC, and although I've never (since his death) visited his grave, I can't leave him there with me across the world in Monaco. So that's it, my old buddy. By the way, you were wrong about one item. We haven't been meeting and writing for 22 years. It's been 25 years since you and I spent the day drinking and talking here in San Diego. Yeah, 25 years, Harry, not 22. I guess that's about all I have to say, Harry, except that I miss seeing you. Maybe this spring ... .

NEVER-ENDING TAX BILL: I guess the whole thing has finally made me angry. I never thought much of the new tax package, and I've said so here many times. The fact is that the boys in Washington never really talked tax reform, what they were discussing was merely tax redistribution. Furthermore, they never talked about a simpler system. All you have to ask yourself is this: How many tax lawyers and accountants is the new tax bill going to put out of business? The answer is none -- not a single one. In fact, I'm beginning to think that the new tax package is going to be messier and more complicated than the horror that we now suffer under.

But the worst thing is that this new tax plan never gets finished. It's become a totally mindless political football. Each day a new set of proposals is made public, and each day the whole thing seems to get more complicated and more exasperating.

So what's happened is that the never-ending tax bill has put investors across the country ON HOLD. Nobody with any money knows what to do. Do you buy munis, do you take stock profits, do you buy T-bonds, do you wait on real estate? I mean it's ridiculous. If it continues, this never-ending tax bill is going to bring business to a screeching halt. Frankly, I don't think I've ever seen such stupidity and incompetence. And it goes on month after month.

I've said before what I think a true simplified income tax bill would be. It would be 17% across the board tax for everybody -- with no exceptions except for muni income and interest on one home -- period. That would bring in as much money as the whole current tax INDUSTRY does, and no one would need a tax lawyer or an accountant. But you know what chance such a truly simplified tax bill would have. Answer -- none! Why? Because it would put the tax industry out of business. And it would bring about screams of unfairness. All right, we'll make one change. Anyone who makes over $60,000 a year pays 19% out of income and that's that. Such a change would bring in even more than the current tax system.

At any rate, I think the proposed tax changes are meaningless, I think they will hurt business, and I think they will prove to be basically deflationary (I call it the "cash and carry tax bill" because it puts more cash in the consumers' pocket, but it eliminates all his write-offs).

But at this point I'm thinking that anything, any redistribution of taxes, is better than the never-ending tax debate. The boys in Congress have succeeded in only one thing -- they've driven investors and the people who have to make decisions to the wall. They've driven them nuts.

OK, ready for my final complaint? What really needs to be done is a massive reduction of the deficits. That's what Congress should be working on, and that's what the nation should be concentrating on. As far as I am concerned, the tax bill is a giant subterfuge. The pressing emergency is the deficit monster. How about getting that one done first -- instead of driving us nuts with the endless tax debate?

NOTES & QUOTES: Again, I want to thank my subscribers for the hundreds of get-well cards and notes received here. I'm feeling much better and am getting stronger by the day. I started walking three days after the open-heart surgery, and now the pain is subsiding. I have orders to take two 20-minute walks per day, but the fact is that I've been up and around for weeks. At the rate I'm going, I'd guess that within six months I'll be my old self again (with the considerable advantage of a much better circulatory system).

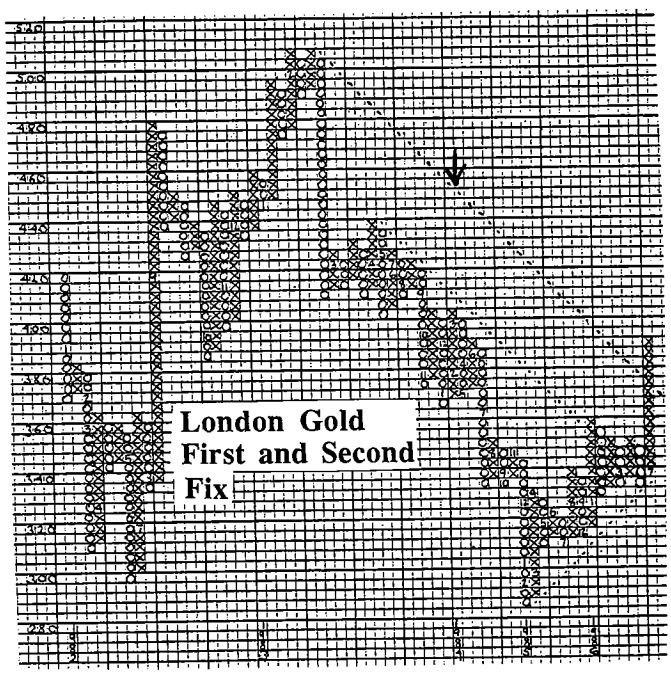
* *

Congratulations to the state of California. Two weeks ago Standard & Poor's raised the bond rating on California state debt from AA to AAA. The state is now running a surplus, and those of us who hold California general obligation bonds are happy. There's nothing like a credit upgrade on debt that you hold to make you feel more secure.

Sanctions: When I was a kid there was an old saying about New York City -- the Italians built it, the Irish ran it, and the Jews owned it. Of course, this old saying was starkly racial, but there was a bit of truth in it. Of South Africa we can say that the blacks built it, the Afrikaners run it, and the English own it. What will sanctions do? Sanctions will make paupers of the blacks, and sanctions will bankrupt the English, who own most of S. Africa's businesses. Ironically, it's the English who are the white liberals in S. Africa (as opposed to the fiercely conservative white Afrikaners). So divestment and sanctions may well destroy the liberal core of S. Africa, the English who have led the fight against apartheid.

* *

Which are the biggest banks in the world? Easy: Dai-Ichi Kangyo Bank is No. 1 with assets of $158 billion, number 2 Fuji Bank with $142 billion, number 3 is Sumitomo Bank with $136 billion and number 4 is Mitsubishi Bank with $133 billion. All four of the world's biggest banks are now Japanese. Oh yes, number 5 is Citibank with $129 billion. ... Last week it was announced that for $500 million Sumitomo was buying a 12.5% stake in the profits of NYC's Goldman Sachs (a leading investment bank). Thus, Japan continues to move BIG into Wall Street. And, of course, Goldman Sachs can use the half billion.



PRECIOUS METALS: Well, it's finally happened! I've been talking about that 364 breakout point for spot gold for so long that I guess it seemed like "the impossible dream" to gold-philes. But on August 8 the London gold fix surged 8 points to 368, and any doubts about the bullishness of the gold picture can now be put aside. As a follow up, on August 11 the London morning gold fix boomed to 394.50.

As you can see on my point & figure chart, gold has now traced out a very bullish basing pattern, a pattern which provides an initial P & F "count" or target of 432 for gold. Note that the main bearish trendline (arrow on chart) has now been REVERSED to the bull side. My gold-to-common stocks ratio (see last Letter) has also reversed in favor of gold, and this provides a bullish (relative strength) background for the precious metals.

I mentioned the desirability of platinum coins in a recent Letter. Here are some facts. South Africa (80.5%) and Russia (8%) together supply 88% of the world's platinum. Canada supplies 5.2% of the world's platinum, and all the other suppliers together are insignificant. Last week platinum broke out above the 500 level, and the metal looks super-strong.

The easiest and, in my opinion, the best way to enter the platinum picture is to buy the Nobles, the one-ounce pure platinum coins minted on the (British) Isle of Man. These coins (which may be ordered from your local coin dealer) are priced roughly 5% above actual (one-ounce) platinum content. I like platinum, I appreciate its strategic importance, and I think it is definitely worthwhile to own some Nobles.

I'm getting a lot of letters asking me about gold mines outside of S. Africa. There are about 2,500 mining stocks in N. America, and in my opinion the vast amount of these are pure crap-shoots, which is another way of saying that they are "worthless." Aside from old faithfuls, Homestake and Campbell Red Lake, there are four good mines in North America, and I guess you could call these the legitimate, blue-chip, non-African gold mining shares. They are Placer Development Ltd., Lac Minerals Ltd., Echo Bay Mines Ltd., and Agnico-Eagle Resources Ltd. Two of these, Placer and Echo Bay, have been making the new high list. Personally, I don't own any mining shares. But I do own gold and platinum coins. I've been accumulating them for months (and I've suggested that my subscribers do the same).

I have said all along that I personally prefer gold coins. Neither gold shares nor gold mutual funds offer the same safety characteristics. Gold, the metal, is subject to A SINGLE VARIABLE, and that is the PRICE of the metal. I like this feature, and I personally don't want to be worried about mine capabilities, mine strikes, politics, etc. So I continue to emphasize the purchase of the metal itself.

There are however, 11 funds, both open-ended and closed-end, that deal in precious metal shares. Two no-load mutual funds that deal in precious metals are Keystone Custodian Precious Metals (800 633 4900) and Lexington Gold Fund (800 526 0056).

Calls are coming in here, and the question asked is "Why, why, why are the metals going up?" Well, first, the metals aren't going up -- gold and platinum are going up. As to why, I think platinum is going up in reaction to the S. African situation. The fact is that the world is using more platinum than it's producing, and platinum users are obviously getting very queasy about the African situation. As for gold, I feel the Japanese, Swiss, Germans and Arabs are buying it as a HEDGE against the huge quantities of US Treasury bonds that they own. As the dollar loses value, foreigners are moving into the gold HEDGE (rather than dumping their T-bonds). Thus gold and platinum climb while the other metals lag. This is not an inflation move in the metals as per 1976-80. This is a different ball game.

LATE NOTES: Well, I keep talking about that 1735.51 low of April 7, and weeks go by, months go by, and the Dow still HASN'T BROKEN BELOW 1735.51 -- which is encouraging action. Nevertheless, it seems as if buying power has diminished on Wall Street (rallies have been unimpressive) and selling pressure, though weak, is in command. When selling pressure expands, the market drifts lower. When selling pressure subsides, the market floats higher. It's been a strange trendless market since July.

Another interesting observation: my PTI, as this is written, is ONLY 20 POINTS BELOW its high for the year. The PTI has really been resisting on the downside, which is impressive. But the biggest problem for this market so far is that no real bearish public sentiment has emerged, despite the general weakness. Thus, we could have listless rallies and unimpressive declines for a while longer. When Wall Street is ready to make its real move, we'll know it. In the meantime, patience ... .

NEXT MAILING: Aug. 27